

Press Release

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TRIS Rating Affirms Company Rating of "DTAC" at "AA+" and Revises Outlook to "Negative" from "Stable"

TRIS Rating has affirmed the company rating of Total Access Communication PLC (DTAC) at "AA+" but has revised the outlook to "negative", from "stable". The rating reflects DTAC's leading market position as the second-largest cellular phone service provider in Thailand in terms of revenue. The credit rating also takes into consideration DTAC's financial strengths, backed by sizable cash flow and sufficient liquidity. The rating is partly enhanced by the support DTAC receives from Telenor ASA (Telenor). However, these strengths are partially offset by the fierce competition in wireless telecommunications services market, DTAC's weaker operating performance, and the large capital expenditures needed to expand coverage.

The "negative" outlook reflects DTAC's weakened operating performance over the past two years due to the fierce competition. Over the medium term, DTAC's financial profile is likely to weaken as a result of lingering, highly competitive market and an expected rise in leverage as DTAC needs to acquire licenses for new spectrum and expand network coverage.

DTAC's rating could be downgraded if the financial profile deteriorates further due to weaker operating performance and/or a rise in leverage. The rating could also be downgraded if DTAC fails to acquire sufficient spectrum to maintain its competitive position. The outlook could be revised back to "stable" if DTAC improves its operating performance while maintaining a strong financial profile. Any change in the degree of support DTAC receives from Telenor will affect DTAC's credit rating as well.

DTAC was incorporated in 1989 and was listed on the Stock Exchange of Thailand (SET) in 2007. Telenor, a leading Norwegian telecommunications company, held directly 42.6% of DTAC's shares as of February 2017. DTAC had 24.5 million subscribers at the end of 2016. The company generated Bt82.5 billion in revenue and about Bt27.3 billion in EBITDA (earnings before interest, taxes, depreciation, and amortization) in 2016.

The rating reflects DTAC's strong market position as the second-largest cellular phone service provider in Thailand, with a revenue market share of around 26% industry-wide. DTAC operates on three frequency bands: 850 megahertz (MHz), 1800-MHz, and 2.1 gigahertz (GHz). Across the three frequency bands, the company holds a total of 50 MHz of spectrum bandwidth. This amount of spectrum bandwidth is adequate to serve its subscribers. A portion of the total (35 MHz) is covered under the concession agreements for the 850-MHz and 1800-MHz frequency bands which will expire in September 2018. The balance of 15 MHz is covered by the license for the 2.1 GHz band valid until 2027. DTAC will be forced to participate in the upcoming bandwidth auctions to ensure it will have ample spectrum to provide services of sufficient quality. As a result, DTAC faces the risks associated with acquiring new spectrum licenses, including plausible high cost of a license, an uncertain timeline of next auction, and regulatory spectrum allocation plan. DTAC must also migrate 2G (second generation) customers to its licensing network before the 2G concession expires. Currently, TOT PLC (TOT), a state-owned telecommunications company, is seeking a partnership to provide wireless broadband services on the 2.3-GHz bandwidth. DTAC is interested in a partnership with TOT. If DTAC is selected as a partner and if the partnership is successful, DTAC will be able to secure additional spectrum bandwidth and significantly reduce the near-term risk over the spectrum capacity.

DTAC's credit rating is strengthened by the support DTAC receives from Telenor, in the areas of managerial assistance and technological know-how support. DTAC is considered significant to Telenor in light of its earnings contribution. DTAC is recognized as top earner in the Telenor Group outside Norway. In recognition of this, TRIS Rating expects that Telenor will support DTAC financially in a time of need.

The rating is partially offset by the fierce competition in the Thai wireless telecommunications services market. Given a saturated and price-sensitive market, all cellular phone service providers are using marketing activities, price packages, and handset subsidies in an effort to maintain their subscriber bases and defend their market shares. As a result of fierce competition, DTAC's subscribers declined from 25.3 million in 2015 to 24.5 million in 2016 due to the aggressive promotions and campaigns competitors used to draw subscribers.

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Further, the rating is constrained by the large capital expenditures needed to expand the network. Each cellular phone service provider needs to make huge capital expenditures to expand coverage of their 4G network. TRIS Rating expects DTAC to make capital investments of roughly Bt57 billion in aggregate during 2017-2019, excluding the cost of new licenses, to roll out its 4G networks nationwide.

DTAC's performance is weaker than peers. DTAC's service revenues (excluding the interconnection charges or IC) fell to Bt64.7 billion in 2016, dropping by 2% from the previous year. The total value of the Thai wireless communications market in 2016 was about Bt245 billion, up 5% from 2015. The market grew at an average annual rate of 3% during the last three years. Conversely, DTAC's service revenues have declined by an average of 2.5% per annum for the past three years. DTAC's operating margin improved from 31.5% in 2015 to 32.8% in 2016, but remains under pressure from the cost to operate two networks: one covered by its licensing network and one covered by concession agreement, large depreciation and amortization charges, and high marketing expenses. DTAC's net profit has declined markedly for two years in successions, arriving at merely Bt2.1 billion in 2016.

Nevertheless, the rating takes into account DTAC's sizable cash flow and sufficient liquidity. Funds from operations (FFO) were sizable in 2016, coming in at Bt23.5 billion, but down from Bt24.8 billion in 2015. The FFO to total debt ratio remains ample, staying at 48% in 2016. However, the ratio dropped from 78% in 2014 and 52% in 2015. Total debt was Bt49.2 billion at the end of 2016. The debt to capitalization ratio was 64.4% in 2016. DTAC had Bt18.3 billion in cash on hand at the end of 2016. The net debt to EBITDA ratio was 1.1 times.

Looking ahead, TRIS Rating is of the view that the market will remain highly competitive, despite a positive prospect driven by the fast-growing demand for mobile data. DTAC's financial profile is likely to weaken as DTAC needs to acquire new spectrum in 2018 while the license cost is expected to be high. A high acquisition cost of a new spectrum is built into TRIS Rating's base case, which is expected to push the leverage ratio to rise over the medium term. During 2017-2019, TRIS Rating expects DTAC's service revenues to remain under pressure, given the intense competition in the market. Any growth in service revenues will be driven by higher data usage and strong demand for data traffic. DTAC is trying to boost the number of postpaid subscribers in an effort to raise average revenue per user (ARPU). Revenue from data services is expected to grow and offset the decline in voice services revenue over the medium term. DTAC's operating margin, despite benefiting from lower regulatory costs, will stay under pressure because of heightened competition and huge depreciation and amortization charges. During 2017-2019, FFO is expected to stay around Bt24-Bt29 billion per annum. The debt to capitalization ratio would sharply rise to about 80%, following a high-priced spectrum. The FFO to total debt ratio is expected to fall to around 25%. However, the actual investment cost for new spectrum is uncertain, subject to several factors, including number of spectrum to offer to the market, degree of bidding competition, and regulatory spectrum allocation plan. TRIS Rating expects DTAC's ample financial flexibility and lower dividend payout will partly help absorb the large investment in network rollout and license cost.

Total Access Communication PLC (DTAC)

Company Rating:

AA+

Rating Outlook:

Negative

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